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In the Supreme Court of the United States

OCTOBER TERM, 1945

No. 835

JOHN E. GALLOIS, EXECUTOR AND JEANNE G. HILL, EXECUTRIX OF THE ESTATE OF MARGARET P. GALLOIS, DECEASED, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Tax Court (R. 89–101) is reported at 4 T. C. 840. The opinion of the Circuit Court of Appeals (R. 120–124) is reported at 152 F. 2d 81.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on November 16, 1945. (R. 125.) The petition for a writ of certiorari was filed on

February 11, 1946. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether Section 811 (c) of the Internal Revenue Code requires the value of the trust corpus to be included in the gross estate of the grantor.

2. Whether there was a "bona fide sale for an adequate and full consideration in money or money's worth", under Section 811 (c), so as to exclude the trust from the grantor's gross estate.

STATUTE INVOLVED

Internal Revenue Code:

> SEC. 811. GROSS ESTATE.
>
> The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—
>
> * * * * *
>
> (c) *Transfers in Contemplation of, or Taking Effect at Death.*—To the extent of any interest therein of which the decedent has at any time made a transfer, by trust or otherwise, in contemplation of or intended to take effect in possession or enjoyment at or after his death, or of which he has at any time made a transfer, by trust

or otherwise, under which he has retained for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death (1) the possession or enjoyment of, or the right to the income from, the property, or (2) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom; except in case of a bona fide sale for an adequate and full consideration in money or money's worth. Any transfer of a material part of his property in the nature of a final disposition or distribution thereof, made by the decedent within two years prior to his death without such consideration, shall, unless shown to the contrary, be deemed to have been made in contemplation of death within the meaning of this subchapter;

* * * * *

(26 U. S. C., Sec. 811.)

STATEMENT

The findings of the Tax Court, so far as pertinent here, are as follows:

The decedent, Margaret P. Gallois, died testate on August 8, 1940, a resident of San Francisco, California. The petitioners, John E. Gallois and Jeanne G. Hill, are executor and executrix, respectively, of her last will and testament. Prior to August, 1924, the decedent had loaned $251,000 to her son, John E. Gallois, with no evidence of

the indebtedness being executed in writing. In order to make this loan she had heavily encumbered her own property. Because she had advanced to her son such a large part of "his portion of the estate", the decedent desired to protect the interest of her other child, Jeanne G. Hill, and accordingly, on August 9, 1924, executed the trust involved herein. (R. 90.)

The trustees were directed to apply the income of the trust, (a) to the payment of interest due or to become due on the obligations of the decedent, secured by liens on the trust property; (b) to the payment of taxes, assessments, insurance, repairs, etc.; and (c) after payment of the above charges, to pay the remainder of the net income to the decedent. (R. 90.) The trustees were also directed to pay any portion of the principal to the grantor which in their opinion might be necessary for her maintenance and support if the income were insufficient. (R. 91.) Upon the death of the grantor, the income was to be paid to her daughter Jeanne for life. (R. 91.) Paragraph "Fifth" made provision for the ultimate distribution of corpus at Jeanne's death, but if Jeanne and all her children should die without issue prior to the grantor's death, the trust was to terminate and the corpus revested in the grantor. (R. 91–92.) Paragraph "Ninth" set forth conditions under which the grantor's son John might share in the corpus after the grantor's death, such condi-

tions being predicated upon John's repayment of the money owed to his mother. (R. 92–93.)

The decedent retained no power to alter, amend or revoke the trust. (R. 93.)

At the time the trust was created, the decedent was 68 years of age and in good health for a woman of that age. She was survived by her two children (Jeanne and John), three grandchildren and three great grandchildren. (R. 93–94.)

The decedent's son was unaware of the trust at the time of its creation and did not learn of its existence until about two years later. (R. 94.)

The husband of the decedent's daughter had been well off, but in the period from 1924 to 1928 he was in very straitened circumstances. It was to protect her daughter from further loss that the decedent had created the trust. The trust had an indebtedness greater than the market value of the property in the trust and decedent's son was constantly being pressed by her son-in-law and others to pay the amount he owed her. He was unable to make any payments on his indebtedness until 1927, but between December 19, 1927, and September 13, 1928, he made payments aggregating about $42,000. (R. 94.)

By October, 1928, decedent's son was financially able to pay the balance of the money he had borrowed from his mother. At that time he and the decedent agreed orally that he would pay back the sums he had borrowed upon condition that he was

made a trustee and that the corpus of the trust would not be invaded again. She agreed to these conditions and her son then executed his promissory note, dated October 30, 1928, in the sum of $251,000, to the trustees. (R. 94.)

On November 7, 1928, two of the original trustees resigned, and decedent's son and daughter were appointed trustees in their place. Following his appointment as trustee, decedent's son paid the balance of his indebtedness. (R. 94–95.)

On June 19, 1942, a California court entered a "Decree Terminating Life Estate, etc." in which it was adjudged that by reason of the death of the decedent an undivided one-half interest in the real and personal property which constituted the trust property vested in her son and the interest of the trust in one-half of the trust estate was terminated. (R. 95.)

The Tax Court held that the entire value of the trust corpus was includible in the gross estate and so found that there is a deficiency in estate tax in the amount of $19,323.36. (R. 101.) Its decision was affirmed by the Circuit Court of Appeals. (R. 125.)

ARGUMENT

1. Under the terms of the trust, the decedent was not only entitled to receive the trust income for life but also to have the principal invaded if necessary for her support. The trust agreement also provided that, if the decedent's daughter

and the latter's children died without issue prior to the death of the decedent, the trust was to terminate and the trust fund was to revest in the decedent. (R. 71, 92.) Because of these rights the decedent had an interest in the trust corpus; and all of the remainder interests, including that of the decedent's son, were contingent. The contingency was not of course removed until the decedent's death, for it could not be known until that time that the beneficiaries of the remainder interests would receive anything from the trust. Indeed it could not be known that the trust would even be in existence until her death. Consequently this case comes squarely within the provisions of Section 811 (c) of the Internal Revenue Code, *supra,* providing for the inclusion of any interest of which the decedent has made a transfer in trust which was intended to take effect in possession or enjoyment at or after her death. *Helvering* v. *Hallock,* 309 U. S. 106. Thus the courts below correctly held that the entire corpus of the trust must be included in the gross estate under that section.

The decision below is supported by *Fidelity Co.* v. *Rothensies,* 324 U. S. 108, and *Commissioner* v. *Estate of Field,* 324 U. S. 113, where this Court held that the entire trust estate in each case was includible in the gross estate. There are no material distinctions in the facts here. In *Fidelity Co.* v. *Rothensies* the decedent had created a trust

to pay the income to herself during her life and at her death to her two daughters during their respective lives. At the death of each daughter the corpus supporting her share of the income was to be paid to her descendants. If both daughters died without leaving surviving descendants, the corpus was to be paid to such persons as the settlor might appoint by will.

The facts are also similar in the *Field* case in that the trust created by the decedent not only reserved the income to him for life but also gave him the right to get back the corpus if he should survive his two nieces. He did not survive them and it was held that the full value of the trust property was includible in his gross estate.

In the *Fidelity Co.* case, this Court announced the rule that the taxable gross estate "must include those property interests the ultimate possession or enjoyment of which is held in suspense until the moment of the grantor's death or thereafter," 324 U. S. at 111. In this connection the Court also pointed out that it makes no difference how remote or uncertain a decedent's reversionary interest may be inasmuch as the decisive factor is whether the possibility of reacquiring the property continues until the decedent's death. To the same effect see *Goldstone* v. *United States*, 325 U. S. 687.

Notwithstanding the above decisions of this Court, petitioners seek to bring the instant case

within the distinctions made in *Commissioner* v. *Irving Trust Co.*, 147 F. 2d 946 (C. C. A. 2d), and *Commissioner* v. *Hall* (C. C. A. 2d), decided January 17, 1946 (C. C. H. Inheritance, Estate and Gift Tax Service, par. 10,253). In the first of these cases, the trustee was authorized to pay over such portion of the trust funds to the grantor (decedent) as the former wished to transfer but payment was absolutely within the discretion of the trustee, and the grantor could collect nothing as a matter of right. Thus the court stated there that since the grantor had reserved no enforcible right and had retained no power or reversionary interest, the situation was distinguishable from that in the *Fidelity* case, *supra*. The *Irving Trust* case does not apply in the Second Circuit where this distinction is absent. *Estate of B. Dominick* v. *Commissioner* (C. C. A. 2d), decided January 2, 1946 (C. C. H. Inheritance, Estate and Gift Tax Service, par. 10,247).

In the *Hall* case the decedent retained the income for life and there was a possibility of reverter by operation of law in the event the decedent survived his own next of kin. The court apparently thought that next of kin was an inexhaustible class (cf. *Engel* v. *Guaranty Trust Co.*, 280 N. Y. 43, 47–48), and held that this did not amount to retention of any right by which the grantor could regain possession or control. In neither the *Hall* nor the *Irving Trust* case was

there a right, as here, to have the principal applied to the maintenance and support of the decedent. Although those decisions may be questionable, there is no reason to believe that the Second Circuit would regard them as controlling here; there is accordingly absent that conflict of decisions between the circuits that requires the intervention of this Court.

2. The petitioners also contend that the portion of the trust estate which passed to the decedent's son comes within the exception in Section 811 (c), permitting exclusion from the gross estate any interest transferred in connection with a "bona fide sale for an adequate and full consideration in money or money's worth." Thus they assert that the decedent's son bought his interest in the trust by paying a debt which he owed to the decedent, the collection of which was barred by the statute of limitations. This payment was allegedly made pursuant to an oral understanding between the decedent and her son that if he would pay the debt she would have him made one of the trustees and would see that thereafter the trustees did not invade the corpus for her maintenance, as they were empowered to do under the trust agreement. (R. 94.) It is apparent, as the Tax Court held (R. 100), that the oral understanding did not refer to, nor in any way concern, the possible invasion of the corpus for the decedent's benefit. It seems clear, too, that no portion of the transfer in trust

was a sale for a consideration, but that the payments constituted the satisfaction of a debt as the Tax Court held. (R. 97.) There is no conflict concerning this question.

CONCLUSION

The decision below is correct and there is no conflict. Accordingly the petition for a writ of certiorari should be denied.

Respectfully submitted,

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